

Student Loans and Code Section 127 Educational Assistance Programs: A Reminder from the IRS, FAQs, and a Sample Plan Document

by Anna Mikhaylina on September 12, 2024

On August 28, the IRS issued [IR-2024-227](#), reminding employers of the following key aspects of educational assistance programs under Internal Revenue Code Section 127:

- They can be used to help reimburse the costs of or pay for employees' student loans through December 31, 2025;
- They must be established in writing and cannot discriminate in favor of highly compensated employees;
- In most cases, benefits under such programs are excluded from federal income tax withholding, Social Security tax, Medicare tax, and federal unemployment (FUTA) tax; and
- Tax-free educational benefits are limited to \$5,250 per employee per year.

Earlier this summer, the IRS also issued [Fact Sheet 2024-22](#) with FAQs regarding educational assistance programs. Of note, the FAQs include a sample plan document that employers can modify to establish an educational assistance program, and they provide protection from penalties based on reasonable, good faith reliance on the FAQs. This post focuses on the student loan aspects of the FAQs and provides actionable steps for employers who offer, or intend to offer, an educational assistance program.

Background

For many years, employers have offered educational assistance programs to assist employees with the cost of tuition, fees, books, equipment, and supplies on a tax-free basis. In 2020, the Coronavirus Aid, Relief, and Economic Security Act amended Code Section 127 to add certain student loan payments to the types of eligible educational assistance available.

The FAQs

The FAQs restate the IRS's prior guidance on educational assistance programs and, for the first time, provide guidance regarding the treatment of student loans. With respect to student loans, the FAQs state that:

- the loans must be incurred by the employee for the education of the employee only, not a spouse or a child of the employee;

- when the loan was incurred does not matter;
- only loans for education at an “eligible educational institution” qualify, and “eligible educational institutions” include:
 - any college, university, vocational school, or other postsecondary educational institution as defined in Code Sections 221(d)(2) and 25A(f)(2);¹
 - an institution conducting an internship or residency program leading to a degree or certificate awarded by an institution of higher education, a hospital, or a health care facility that offers postgraduate training;²
- only student loan debt incurred for tuition, fees, books, equipment and supplies qualifies;
- loan payments paid or reimbursed by the employer must be made during the period beginning March 28, 2020 and ending December 31, 2025 (unless extended by future legislation) and may be paid directly to a third party such as an educational provider or a loan servicer, or directly to the employee;
- if an employee seeks reimbursement for student loan payments, the payments must be paid by the employee while an employee and in the same calendar year for which reimbursement is made by the employer;
- the total amount that the employee can exclude from gross income for payments of principal or interest on student loans and other educational assistance under Code Section 127 is \$5,250 per calendar year; and
- “unused” amounts of the \$5,250 annual limit cannot be carried forward to subsequent years.

For example, an employer may reimburse an employee in 2025 for the payments made in 2025 on student debt incurred by the employee in 2015 prior to employment if the other requirements described above are satisfied, but an employer cannot reimburse the employee after 2025 for any student loan payments.

¹ The Department of Education determines whether an organization is an eligible education institution. A loan, however, does not have to be issued or guaranteed under a Federal postsecondary education loan program to be a qualified education loan.

² Code Section 221(d)(2)(B).

Reliance on FAQs

The IRS expressly states in Fact Sheet 2024-22 that:

- taxpayers who rely in good faith on the FAQs will satisfy the reasonable cause standard for penalty relief, and
- if an FAQ turns out to be an inaccurate statement of the law as applied to a particular taxpayer's case, the law will control the taxpayer's tax liability, not the FAQs.

What should employers do?

Employers who offer, or intend to offer, an educational assistance program should:

- maintain a written plan and provide reasonable notice of the availability of the program to employees;
- if providing student loan assistance as part of the program, ensure the terms of the plan reflect that; and
- review the IRS [sample plan](#), which includes: (1) optional provisions that allow the employer to choose whether or not to include student loans as an educational assistance benefit under the plan; and (2) mandatory provisions describing non-discrimination and substantiation requirements.

As a design matter, employers may also want to consider limiting eligibility for the program to employees who are not highly compensated as defined by Code Section 414(q).³ This will dramatically simplify administration of the program because the program would automatically pass required non-discrimination testing.⁴

Overall, the reminder, the FAQs, and the sample plan document are valuable tools for employers that have established, or are looking to establish, educational assistance programs.

Anything else about student loans?

For plan years beginning after December 31, 2024, SECURE 2.0 allows employers to make matching contributions to certain retirement plans based on qualified student loan payments by employees. Our August [post](#) describes in detail the IRS guidance on this change in the law.

³ Generally, an employee who: (1) during the current plan year or the preceding plan year was at any time a more than 5% owner of the employer; or (2) received compensation from the employer for the preceding plan year in excess of \$150,000 (for 2024) is a highly compensated employee for the current plan year.

⁴ Note, there is an additional limit relating to more than 5% owners of the employer: not more than 5% of the amounts paid or incurred by the employer for educational assistance during the year may be provided for such individuals (or their spouses or dependents), considered together as a group.



If you have any questions regarding Code Section 127 educational assistance programs, including the student loan feature, please contact a member of our [Employee Benefits & Executive Compensation Group](#).



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